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No.

IN THE

Supreme Court of the United States

October Term, 1982

Span-Deck, Inc.,
Petitioner,

v.

Fabcon, Incorporated and Rauenhorst Corporation,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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QUESTIONS PRESENTED

I. What is required by the relationship between federal patent law and state contract law when two patents constitute part, but not all, of the consideration for a contract awarding a franchise and one of the patents is declared invalid: does federal patent policy bar a state from enforcing a franchise contract despite the presence of other substantial consideration for the franchise, including another patent which is valid?

II. Does the mere assertion of patent invalidity as the reason one induced another to breach a franchise contract require that the question of justification for inducing breach of contract be removed from jury consideration, despite state law requirements of proof of actual motivation, good faith, and other factors before the defense of justification is established?

III. In reviewing factual findings of a jury, is a court of appeals permitted to employ a standard of review different from the substantial evidence standard, despite the precepts of the Seventh Amendment and efficient judicial administration, and instead make its own independent factual findings, contrary to those of the jury, concerning:

(a) the facts underlying the question of obviousness in a determination of patent validity, where most other courts of appeals require a substantial evidence standard of review;

(b) the facts concerning the defense of justification against a claim of tortious inducement of breach of contract; and

(c) the facts establishing whether a franchise contract was automatically renewed in accordance with its terms?

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

Span-Deck, Inc. ("Span-Deck")[1] respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eighth Circuit entered in this case on May 12, 1982.

OPINIONS BELOW

The opinion of the district court (App. B) dated July 21, 1982 is unreported. The opinion of the court of appeals (App. A) is reported at 667 F.2d 1237 (8th Cir. 1982).

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[1]Span-Deck Inc. is a wholly-owned subsidiary of the St. Regis Paper Company. Span-Deck has no subsidiaries, and the domestic subsidiaries of St. Regis are listed in Appendix I.

JURISDICTION

On May 12, 1982, the court of appeals entered an opinion (App. A) vacating the judgment of the district court and reversing and remanding the matter for further proceedings. Span-Deck filed a timely petition for rehearing on May 26, 1982. The petition for rehearing was denied on June 7, 1982 (App. F). This Court has jurisdiction to review the judgment of the court of appeals by writ of certiorari pursuant to 28 U.S.C. §1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Set forth in Appendix H are pertinent provisions of the Seventh Amendment to the Constitution of the United States and the Patent Act, 35 U.S.C. §§ 103, 112, and 282.

STATEMENT OF THE CASE

This case involves an attempt to enforce a franchise contract, and to collect damages for its breach and for the wrongful inducement to breach the contract. The jury and the district court found in favor of Span-Deck and awarded compensatory damages of $1.5 million and punitive damages of $2 million.

The Court of Appeals for the Eighth Circuit reversed the judgment of the district court. It concluded, on the basis of its own factual findings, that one of the patents which had been licensed under the franchise contract should have been found invalid by the jury and the district court; that since it had found the patent invalid, a franchise contract which referred to it could not be enforced because to do so would be inconsisent with feder-

al patent policy; and that conduct in inducing the breach of the franchise contract was justified by the assertions of patent invalidity, without regard to actual motivation or good faith.

The remand of the court of appeals recognized the value and transfer of trade secrets, another valid patent, and other non-patent consideration for the franchise contract, but remanded for a determination of the value of nonpatent rights and damages for misappropriation of trade secrets rather than enforcement of the contract.

A. The Span-Deck Process, Trade Secrets and Related Patents.

The Span-Deck franchise contract enables one to engage in the manufacture of prestressed, precast hollow core concrete plank. The Span-Deck franchise is one of several competing franchise systems for the casting of such plank. It is the hollow core feature of such plank which makes the concrete panels sufficiently lightweight and inexpensive to be competitive with other building materials. The means by which the hollow cores are formed is among the items which distinguishes Span-Deck from its competitors. Span-Deck's method and equipment are protected by its trade secrets. It has also acquired two patents covering certain aspects of its equipment: one issued in 1965 to Claiborne Kinnard, and another issued in August, 1970, to William Mitchell.

Claiborne Kinnard developed an apparatus and method wherein a moving casting machine deposits liquid concrete around cores of lightweight granular core material, which passes through slipforms shaping the cores. The slipforms simultaneously shape the liquid concrete to sur-

round highly tensioned steel cables extending from end to end of a stationary casting bed. Enormous tensile forces and weights are necessarily involved. The planks are manufactured as continuous hollow bodies in long casting beds. After curing, individual planks are cut from these long beds. The cores are made hollow by dumping out the granular core material after the concrete has hardened.

William Mitchell's improvement on Kinnard's invention fixed the casting apparatus in place and devised a means by which the bed upon which the concrete was placed could be moved as required for various plank production steps. This improvement solved the even greater material handling problems which arose when wider and longer casting beds were employed, requiring a precise means for moving and controlling a large casting bed in coordination with the stationary casting, curing, cutting, bed stripping, and bed cleaning equipment, and the stockpiling and centralized use of the production materials.

B. The Span-Deck Franchise System.

Since the beginning in 1964, each franchise contract has taken the form of a technical assistance agreement licensing unpatented experience and knowledge, know-how and trade secrets, and trademarks. When the patents were issued in 1965 and 1970, franchise contracts also included rights under those patents.

The Span-Deck franchise fee was established in 1964 before it had any patents, and it has never been adjusted for any reason, except for an inflation increase in 1980. The franchise fee under the contracts entered into before

Span-Deck had any patents required a royalty of three cents per square foot of plank produced, declining with higher production. The franchise fee under the contracts entered into after each patent issued required the *same* royalty, which was not raised or altered in any way in 1965 or 1970 when Span-Deck acquired its patents.

By the summer of 1970, when negotiations for the Span-Deck/Fabcon franchise contract began, Span-Deck had 30 outstanding franchise contracts and had completed installation of approximately 20 plants in the U.S. and Canada, all requiring the same royalty rate.

C. The Breach of the Franchise Contract.

Span-Deck and Fabcon, Incorporated ("Fabcon") entered into a franchise contract (App. G) on October 7, 1970. Fabcon prospered under its Span-Deck franchise. It was in commercial operation within ten months of signing the contract. It doubled its capacity a year and a half later.

In spite of its financial success, early in 1972 Fabcon and Rauenhorst Corporation ("Rauenhorst"), of which Fabcon is a wholly-owned subsidiary, began to take steps to avoid the obligations under the franchise, steps which were inconsistent with the contract. These actions began about one year before the cessation of royalty payments in 1973.

In March, 1972, David Hanson, Fabcon's President, wrote to a business associate that he was not promoting his plant's products as Span-Deck planks, but rather as "Fabcon slabs", contrary to Paragraph 3.5 of the franchise contract (App. G, p. A-76). In August, Fabcon tried to hire Larry Foster, a key Span-Deck engineer. In Sep-

tember, Hanson wrote a memorandum to Gerald Rauenhorst, President of Rauenhorst Corporation, discussing methods "[t]hat might be a way to get out of the royalty." In November, Hanson took steps to keep process improvement information from being disclosed to Span-Deck as required by Paragraph 4.5 of the franchise. (App. G, p. A-78). The continued success of this effort to withhold information was reported to Rauenhorst in late February, 1973.

Fabcon made its last royalty payment to Span-Deck in January, 1973, covering December, 1972 production. At first, Fabcon offered no explanation. On March 5, 1973, Hanson wrote that Fabcon had stopped paying because Fabcon was supposedly entitled to a credit under a "most-favored-licensee" clause of the franchise contract. In fact, Fabcon was having cash flow problems when it stopped paying royalties.

On April 30, 1973, Gerald Rauenhorst met with Ed McMahon, an officer of Span-Deck's parent company. Rauenhorst proposed termination of the franchise, claimed that Span-Deck's patents were invalid or not infringed, and threatened to tell other franchisees of his position if the franchise contract was not terminated. (This is the only evidence that cessation of royalty payments had any relationship to patents). In a subsequent telephone conversation, McMahon told Gerald Rauenhorst that Fabcon had "a franchise agreement above and beyond the patents" and that Span-Deck had certain rights and obligations under the franchise.

D. Commencement of Suit.

Fabcon continued in its refusal to pay royalties, but also continued to exercise its privileges under the fran-

chise contract. Span-Deck did not agree to terminate the franchise. It brought suit against Fabcon and Rauenhorst in the United States District Court for the District of Minnesota on November 1, 1973.[3] Span-Deck's primary claims, stated in Counts I and II of its Complaint, were for breach of the franchise contract, and for tortious inducement of the breach.[4]

The Answer and Counterclaim generally denied the principal allegations in the Complaint and asserted affirmative defenses as to the alternative claims for patent infringement. It also sought a declaratory judgment that the franchise contract was not valid or enforceable due to alleged failure of consideration by reason of the alleged invalidity of the Kinnard and Mitchell patents.

At the time this suit came to trial late in 1980, Span-Deck had 40 active franchises, including franchises in such foreign countries as Canada, Hungary, Finland, Spain, Japan, Dubai, Australia and Venezuela. Other than Fabcon, no franchisee has ever asserted patent invalidity, nor sought to avoid its franchise contract obligations to Span-Deck.

E. The Results of the Jury Trial and Post-Trial Motions.

After extensive discovery and pretrial motions, the matter was tried to a jury of ten persons[5] commencing on

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[3]The district court's jurisdiction was based on 15 U.S.C. § 1121, 28 U.S.C. §§ 1332(a), (c), and (e), and 28 U.S.C. §§ 1338(a) and (b).

[4]The complaint also contained alternative counts applying to any time in which it might be determined that the contract between Fabcon and Span-Deck was not in effect by reason of expiration, cancellation or invalidity. Count III: unauthorized use of Span-Deck's trade secrets; Counts IV and V: infringement of Span-Deck's trademarks (Counts IV and V were withdrawn before the matter was submitted to the Jury); Count VI: infringement of the "Mitchell" patent; and Count VII: infringement of the "Kinnard" patent.

[5]By agreement of counsel, the alternate jurors and the original panel participated and deliberated as jurors in reaching the verdict.

November 17, 1980. On February 9, 1981, after almost forty days of trial, the jury was charged and presented with 22 Special Verdict questions. After a week of deliberation, the jury returned with its answers to the Special Verdict form (App. C).

After ruling on post-trial motions, on July 21, 1981, the district court entered its Memorandum and Order (App. B). That judgment enforcing the jury's Special Verdict awarded compensatory damages of $1.5 million against Fabcon and Rauenhorst for breach of contract, and exemplary damages of $2 million against Rauenhorst for inducement of the breach; the Kinnard patent, though valid, was held not infringed by the equipment used by Fabcon. The Mitchell patent was held valid and infringed.

F. The Decision of the Court of Appeals.

Defendants appealed from the judgment of the district court. In an opinion dated May 12, 1982, a divided panel of the Court of Appeals for the Eighth Circuit vacated the judgment of the district court and reversed and remanded the case.

The court determined that federal patent policy barred enforcement of the Span-Deck/Fabcon franchise contract because it included rights under an invalid patent among the benefits conferred by the contract. It also determined that the mere assertion of patent invalidity was sufficient to remove the question of justification for inducing the breach of contract from jury consideration, despite state law requirements of proof of actual motivation, good faith, and other factors.

In reaching these conclusions, the court determined that

the Mitchell patent should have been held invalid, and reversed other factual determinations, based on its own view of the facts, which was contrary to the findings of the jury as separately confirmed by the trial court.

Finally, the court of appeals affirmed the validity of the Kinnard patent and remanded "for a determination of the value of nonpatent rights received by Fabcon from the time Fabcon ceased payment of royalties until termination of the contract on October 6, 1975," and "a determination of damages for misappropriation of trade secrets after the contract termination." (App. A, p. A-27).

REASONS FOR GRANTING THE WRIT

I.

When A Patent Constitutes Part, But Not All, Of The Consideration For A Franchise Contract, Federal Paent Policy Does Not Bar A State From Enforcing The Contract Where Other Substanial Consideration, Including Trade Secrets And Another Valid Patent, Is Present, And The Court Of Appeals Decision To The Contrary Warrants Review By This Court.

In denying enforcement of the franchise contract between Span-Deck and Fabcon, the court below justified its decision primarily by reference to *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969). In doing so, the court below improperly extended *Lear* beyond its holding that a patent licensee is not estopped to challenge the validity of a licensed patent and may withhold royalties while doing so. The result is an unwarranted preemption, in the name of federal patent law, of state contract law permitting the enforcement of otherwise valid contracts. The scope of the rule pronounced

in the decision of the court below jeopardizes a large class of existing legitimate business relationships and discourages parties from entering into franchises or technical assistance agreements where a patent or patent application covers a portion of the technology involved. It is also likely to discourage use of the patent system.

A. Prior Decisions of This Court Require That a Proper Accommodation be Struck Between Federal Patent Law and State Law so that State Law Is Only Preempted When it Stands as an Obstacle to Achieving the Purposes of Federal Patent Law.

The history of this Court's recent decisions delineating the proper relationship between federal patent law and state law shows the difficulty and importance of mapping out the area of preemption so as to adequately balance the interests of federal patent law against the compelling tradition that parties are free to contract for patent or other intellectual property rights in exchange for mutually agreed compensation. Although not first in time among those decisions, *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470 (1974), perhaps best exemplifies the standards which this Court has used to determine the proper accommodation between federal patent law and state law when the two appear to clash. In *Kewanee*, the Court held that state trade secret protection was not preempted by operation of the federal patent law. In reaching this conclusion, the Court analyzed the objectives of both the federal and state laws, *see* 416 U.S. at 480-482, and examined the interaction of the two systems, *see id.* at 482-492, before determining whether and under what circumstances preemption might apply. The *Kewanee* Court thus both ruled

that state law is not automatically preempted by patent law in the area of protection of intellectual property and set forth by example the kind of analysis which must underlie a decision that state law is preempted. The summation of that analysis is the standard that state law governs except to the extent that it stands as an obstacle to frustrate the policies of the federal patent law.

This general standard exemplified by *Kewanee* underlies the Court's other recent decisions as well. Thus, in *Brulotte v. Thys Co.*, 379 U.S. 29 (1964), the Court examined contracts involving licensing of patented hop picking equipment in exchange for royalties based on use or production. The contracts provided that royalties were to be paid beyond the life of the patents involved. The Court held that such contracts extended the patents unlawfully and were unenforceable as to post patent expiration royalties. The conflict between the limited seventeen year patent term and the extended royalty obligation made preemption necessary.

In *Lear v. Adkins, supra,* the Court was asked to rule on the viability of the doctrine of licensee-estoppel, which had been invoked by a licensor to try to force a licensee to pay royalties while the licensee challenged the license on the issue of patent validity. The court specifically found requiring continued payment of royalties to be "inconsistent with the aims of federal patent policy." 395 U.S. at 673. It referred to the importance of giving patent licensees an economic incentive to challenge patents. The case also involved a claim for contractual royalties due before the patent issued, i.e., during the period when the licensed technology was an unpatented secret idea. The Court concluded

> "that even though an important question of federal law underlies this phase of the controversy, we should not now attempt to define in even a limited way the extent, if any, to which the States may properly act to enforce the contractual rights of inventors of unpatented secret ideas."

395 U.S. at 675. Justice White, concurring in part, focused even more directly on the federal law-state law tension presented by the case:

> One of the defenses presented by Lear in its answer to Adkins' claim for royalties was that there had been a failure of consideration because of the absence of bargained-for patentability in Adkins' ideas. But failure of consideration is a state law question, and I find nothing in the record and nothing in this Court's opinion indicating that Lear at any time contended in the state courts that once Adkins' patent was invalidated the royalty agreement was unenforceable as a matter of federal law.

395 U.S. at 679 (footnote omitted).

In *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257 (1979), the Court had occasion to examine another decision by the Eighth Circuit which, like the one here presented to this Court for review, also involved an interpretation of the rule in *Lear*. In *Aronson*, a licensee challenged its duty to pay royalties under a license contract when the licensor's invention, originally licensed as a trade secret, failed to achieve patent protection. The contract contemplated continued royalties at a reduced rate were no patent obtained and without regard to the fact that no trade secret existed once the licensed keyholder was sold. The licensee argued that the *Lear* case prevented enforce-

ment of the contract. The district court had held the contract valid, while the Eighth Circuit held it invalid, based on *Lear*. In its consideration, this Court noted that the matter again called for a resolution of tension between state contract law and federal patent law:

> Commercial agreements traditionally are the domain of state law. State law is not displaced merely because the contract relates to intellectual property which may or may not be patentable; the states are free to regulate the use of such intellectual property in any manner not inconsistent with federal law.

440 U.S. at 262 (citations omitted). After weighing the effect enforcement of such a contract would have on the policies of patent law, this Court concluded that federal law was no barrier to contract enforcement.

In its preemption analysis in *Aronson*, the Court reviewed the same purposes of the federal patent system which it had identified in the *Kewanee* case:

> First, patent law seeks to foster and reward invention; second, it promotes disclosure of inventions to stimulate further innovation and to permit the public to practice the invention once the patent expires; third, the stringent requirements for patent protection seek to assure that ideas in the public domain remain there for the free use of the public.

440 U.S. at 262. After analyzing the effect of enforcement of the Aronson-Quick Point contract on each of the purposes, the Court concluded that the contract was not inconsistent with any of these aims.

Aronson thus stands for the proposition that, where the parties separately stated in the contract what non-

patent consideration was involved in the event patent-based consideration failed, federal patent law did not require that the contract be voided. "The cases and principles [including the *Lear* rule] relied on by the Court of Appeals and Quick Point do not bear on a contract that does not rely on a patent, particularly where, as here, the contracting parties agreed expressly as to alternative obligations if no patent should issue." 440 U.S. at 262. Although hinting at the appropriate result even where no such express statement of alternative consideration has been made, the Court did not rule on the appropriate result in a situation where a patent forms only a part of the contract consideration but the parties have not expressly apportioned the consideration involved.

B. The Decision of the Court Below is Based on the Erroneous Concept of a Hybrid Royalty Rather Than a Proper Preemption Analysis.

The question which this Court did not have to reach in *Aronson* was presented to the Eighth Circuit in this case. Even as it had done in *Aronson*, the Eighth Circuit answered the question by looking to its erroneous interpretation of *Lear* rather than engaging in the kind of careful analysis exemplified by *Kewanee* and reiterated in *Aronson*.

The court of appeals' initial error was failing to clearly identify and give proper consideration to the result required by state law. In particular, the decision simply sets to one side the jury's finding that the contract was supported by considerations other than patents. (See App. C, p. A-57). The decision also overlooks the facts that *two* patents were licensed, that only one was found invalid, and

that Fabcon also received trade secrets and continues to use them. It also overlooks the other technical assistance materials and services and the trademark rights provided in paragraphs 2.1 to 2.7 of the contract (App. G, pp. A-71-A-73). Thus, the franchise is clearly supported by consideration, even if the Mitchell patent is, ultimately, held invalid. Under these circumstances state contract law would recognize a valid contract and require that the promised royalty be paid in full. *See, e.g.*, 17 C.J.S. *Contracts* §§ 130-131 (1963 & Supp. 1982) and cases cited therein.

These matters of consideration and enforceability were not addressed by the court below. More importantly, the consequences of enforcing such a contract were not tested to see if they actually stand as obstacles to the goals of federal patent policy, as required before finding preemption. *See, Hines v. Davidowitz*, 312 U.S. 52, 67 (1). Instead, the Eighth Circuit made the same type of error which required reversal in *Aronson*: the court assumed that *Lear* requires the invalidation of any contract which contemplates a valid patent if no such patent obtains.

The analysis of the court below was based on the concept of a "hybrid royalty", which appears to have been derived from the case of *St. Regis Paper Co. v. Royal Industries*, 552 F.2d 309 (9th Cir.), *cert. denied*, 434 U.S. 996 (1977), as an extension of the *Lear* case. In the *St. Regis* case, a licensor sought recovery of royalties under a license involving a single patent and know-how. The patent was held invalid. The license was rescinded due to the invalidity and because the inventor was held to have knowledge of the patent's invalidity, which was imputed to the licensor. Nevertheless, the licensor argued that the royalty obligation could not be terminated as to know-how because the termination notice required by the license was not

given. When the licensor attempted to collect half the contractual royalty based on know-how received by the licensee, the Ninth Circuit examined the termination provision and found the patent rights and the know-how "so intimately intertwined . . . that the same rule which makes royalties for patent rights uncollectible if the patent is invalid should apply with equal force to know-how." 552 F.2d at 315. The provision requiring notice of termination was thus held unenforceable both for patent rights and for know-how. The Ninth Circuit denied the licensor's know-how royalty claim and approved the district court's determination that the licensor's compensation for the value of the know-how was covered by previously paid royalties. While the Ninth Circuit cited *Lear*, its preemption analysis was limited to consideration of the *licensee's* claimed restitution remedy. It did not measure the effect of enforcing the contract as to nonpatent consideration against the purposes of federal patent law but rather against the intent of the parties in their termination provision.

In the instant case, the court below took *Lear*, together with *St. Regis*, as grounds for condemning all contracts in which the royalty is "hybrid" in the sense that a patent forms any part of the consideration for the contract. It concluded that allowing enforcement of any such contract would prevent the "unmuzzling" of royalties to aid licensees in patent challenges in accordance with *Lear*. (App. A, p. A-23). This rule is too broad. It fails to strike a reasonable and reasoned balance between state contract law, which supports the expectation that a contract will be enforceable, and the purposes of federal patent law. The rule stated by the court below is not required by the *Lear* case, nor is it consonant with the *Kewanee* or *Ar-*

onson cases, which show the manner in which a preemption analysis must proceed. The *Kewanee* case, which upholds an entire body of state trade secret law as against a claim of preemption by federal patent law, not only sets forth the required analysis but, *a fortiori*, states the required result. *See Aronson, supra*, 440 U.S. at 265.

To paraphrase this Court's observation in *Aronson*, "[n]o decision of this Court relating to patents justifies relieving [Fabcon] of its contract obligations." 440 U.S. at 264. No attempt is made here to extend a patent beyond its 17 year life. *Cf. Brulotte, supra.* No state law doctrine prevented Fabcon from challenging the validity of the patents or from suspending the payment of patent royalties pending the outcome of that challenge. *Cf. Lear, supra.* On the other hand, the Eighth Circuit's "hybrid royalty" rule, derived not from the *Kewanee* analysis but from the Eighth Circuit's own misapprehension of *Lear*, represents an unwarranted intrusion into state contract law not consistent with the principles of our federalism articulated in *Kewanee* and *Aronson*.

C. The Decision Below Will Have Far-Reaching Effects on Franchises, Technical Assistance Agreements and the Patent System.

If contracts such as the present one are held unenforceable, the impact of such a decision would be far-reaching. First, Span-Deck's other similar contracts would appear subject to the same rule. Second, every company which has a franchise or technical assistance agreement involving a "hybrid royalty" to be paid in exchange for a license of rights to one or more patents in combination

with other consideration' will face challenges from licensees who are aware of the long list of available patent invalidity defenses and who wish to stop paying royalties by, in effect, asking a federal court to renegotiate their bargain. Third, parties who license a package of unpatented technology will be discouraged from pursuing patent protection, if the protection sought is anticipated to be part of their licensed subject matter. Fourth, parties who plan to license a technical assistance package including patented technology will look for artificial ways to keep patent rights out of their agreement, lest the entire bargain be later challenged, based on an invalidity claim against the patent license portion of the consideration. Fifth, parties who license a technical assistance package including patents will be forced to artificially segregate patent and non-patent consideration, with separate royalties for each.

The Eighth Circuit's woodenly derived and erroneous answer to the question left open by *Lear* and *Aronson* thus stands as a foreboding precedent in a very significant field. The jurisdiction of this Court should be exercised to affirm the procedures for determining preemption previously stated by this Court and to clearly define the extent to which federal patent law may preempt state contract law to deny enforcement of a contract supported by consideration other than a patent later declared to be invalid.

'The frequent use of such arrangements is seen in Eckstrom, *Licensing In Foreign and Domestic Operations*, §18.04 "Technical Assistance Agreements" and §18.05 "Combination License Agreements," reprinting a number of examples of agreements in which one party provides and licenses a broad package of proprietary rights including patent rights.

II.

The Court of Appeals' Decision that the Mere Assertion of Patent Invalidity as the Reason One Party Induced Another to Breach a Contract Requires Removal of the Question of Justification from the Consideration of the Jury and the Requirements of State Law is an Unwarranted Extension of Federal Preemption Which Merits this Court's Review.

The decision of the court of appeals to rely on the *Lear* case also led to its reversal of Span-Deck's judgment against Rauenhorst for interfering with the contract between Span-Deck and Fabcon. The court of appeals established Rauenhorst's justification defense as a matter of law. It concluded that since cessation of royalties was justified under *Lear*, Rauenhorst's actions were "justifiable under the circumstances" and that a directed verdict or j.n.o.v. should have been granted in its favor (App. A, p. A-19).

This decision had the effect of preempting state tort law under which liability for interference with contract is established, but the court of appeals, ignoring *Kewanee*, failed to consider whether federal patent policy required such preemption.

A. Under Minnesota Law the Existence of Justification for Inducing Breach of a Contract is a Jury Question.

Minnesota law on the issue of justification inducing breach of contract is clear. First, justification is an affirmative defense, and the burden of proof is on the party accused of inducing breach. *Johnson v. Raade*, 293 Minn.

409, 196 N.W.2d 478 (1972); *Royal Realty v. Levin*, 244 Minn. 288, 69 N.W.2d 667 (1955); *Carnes v. St. Paul Union Stockyards Co.*, 164 Minn. 457, 205 N.W. 630 (1925). Second, what constitutes justification in a specific case is for the jury to decide. Minnesota courts have not attempted to formulate a rule by which justification or lack of justification may be determined, but have said that in general the issue is largely one of fact for the jury, the standard being reasonable conduct under all the circumstances of the case. *Bennett v. Storz Broadcasting Co.*, 270 Minn. 525, 537, 134 N.W.2d 892, 900 (1965). *Accord, Royal Realty v. Levin, supra; Carnes v. St. Paul Union Stockyards Co., supra.* The Eighth Circuit has acknowledged that justification is a jury issue in Minnesota. *Smith v. American Guild of Variety Artists*, 349 F.2d 975 (8th Cir. 1965) *vacated and remanded for reconsideration on other grounds*, 384 U.S. 30, *original opinion re-adopted and re-affirmed in all respects*, 368 F.2d 511 (8th Cir. 1966), *cert. denied*, 387 U.S. 931 (1967); *American Surety Company v. Schottenbauer*, 257 F 2d 6 (8th Cir. 1958).

B. The Decision of the Court Below Removes the Question of Justification from Jury Consideration Contrary to Minnesota Law and Without Support in Principles of Preemption.

The court of appeals concluded that interference with the contract was justified by *Lear*. This is contrary to the approach taken by this Court in *Kewanee*, which, rather than merely invoking *Lear*, carefully evaluated federal patent law policy against the particular state tort law involved. Nor can it be assumed that whatever mat-

ters of federal patent policy the court of appeals relied on to preempt Span-Deck's contract claim would be equally applicable to the tort claim for interference. It is also a principle of Minnesota law that the issue of justification involves consideration of the defendant's good faith. *Wolfson v. Northern States Management Co.*, 210 Minn. 504, 299 N.W. 676 (1941). Even if *Lear* might, as a matter of legal principle, be available as a justification for a party inducing breach, the jury question of whether this claimed justification was the good faith motive of the defendant remains.

Use of the *Lear* case in the manner chosen by the court of appeals establishing a scope of preemption for federal patent law which has serious consequences for tort law in Minnesota and other states. Whether such a decision can be supported by principles of federal preemption is a question which merits consideration by this Court. This is particularly so because it affects parties' rights to have their cases determined by juries.

III.

The Court of Appeals' Violation of the Substantial Evidence Standard of Review of Factual Findings by a Jury, Which Standard is Mandated by the Seventh Amendment and the Efficient Administration of Justice, and Its Substitution of Its Own Independent Fact Findings on Several Critical Matters Call for Review by This Court.

The decision below rests on three key fact findings, findings made independently by the court of appeals in direct contradiction to the facts as determined by the jury and separately confirmed by the trial court, following

eight weeks of trial. First, the court of appeals found the Mitchell patent invalid on grounds of obviousness. *(See* App. A, p. A-16). Without this finding, even under the Eighth's Circuit reasoning, the franchise contract would be enforced under principles of state contract law. Second, the court of appeals found that Rauenhorst was not liable for inducing Fabcon's breach of contract, because its conduct in encouraging Fabcon not to pay royalties was justified.[6] *(See* App. A, p. A-19). Third, the court of appeals found that the franchise contract was not renewed in accordance with its terms. (*See* App. A, pp. A-23-A-26).[7]

Each of these contradictions of jury-determined facts was the direct result of use by the court of appeals of an

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[6]This finding is discussed in Section II, *supra.*

[7]The court of appeals overturned the jury's finding as to renewal of the franchise contract, reaching its own factual determination that the franchise terminated on October 6, 1975. Although the court of appeals excused this incursion into the jury's province by its conclusory denomination of the questions as matters of law, the trial court in fact acted properly in giving the jury the responsibility of finding whether a proper notice of termination had been given or whether Fabcon's actions inconsistent with the notice caused waiver of the right to prevent automatic renewal. *See U.S. for Use and Benefit of Smith v. Maryland Casualty Co.* 146 F.2d 379, 381 (5th Cir. 1946); *Kennedy v. Hasse,* 262 Minn. 155, 160-161, 114 N.W.2d 82 (1962); *Maloney v. Madrid Motor Corp.,* 385 Pa. 224, 122 A.2d 694 (1956). The jury considered whether the supposed notice was not really any notice of termination at all but rather one more move in the Fabcon/Rauenhorst strategy to refuse to pay Span-Deck any royalties while continuing to enjoy benefits made available only because they had entered into the franchise contract.

At trial there was evidence showing that the provisions of the franchise contract made Fabcon's purported notice of termination ineffective because the right to prevent automatic renewal was forfeited by Fabcon's default and because the parties intended that termination actually be accompanied by a wind-down in manufacturing and cessation of use of Span-Deck's proprietary rights pursuant to paragraph 4.4 of the contract. (*See* App. G, p. A-78). The trial court properly gave these questions to the jury. *Rankin v. Fidelity Trust Co.,* 189 U.S. 242 (1903); *Singer Co. v. E. I. duPont de Nemours & Co.,* 579 F.2d 433, 439-440 (8th Cir. 1978); 3 Corbin, *Contracts* § 554 (1960).

incorrect standard of review on appeal. These appellate errors are of serious magnitude both because they contravene constitutional principles and because they seriously affect the administration of justice and the perception thereof.

A. The Correct Standard of Review Is of Both Constitutional and Juridical Importance.

As this Court has long recognized, "[a]ppellate review in the federal courts is, of course, limited ultimately by the Seventh Amendment." *Lumbermen's Mutual Casualty Co. v. Elbert*, 348 U.S. 48, 53 n. 5 (1954), citing *Parsons v. Bedford, Breedlove & Robeson*, 28 U.S. (3 Pet.) 433 (1830).

> We might agree with the Court of Appeals had the question of fact been left to us. But neither we nor the Court of Appeals can redetermine facts found by the jury any more than the District Court can predetermine them. For the Seventh Amendment says that "no fact tried by a jury, shall be otherwise reexamined in any Court of the United States, than according to the rules of the common law."

Atlantic & Gulf Stevedores, Inc. v. Ellerman Lines, Ltd., 369 U.S. 355, 358-359 (1962).

The correct standard to be applied for appellate review of jury-determined facts is thus a matter of constitutional importance. It is also a matter important to the effective administration of justice. Standards of appellate review which, by their terms or in application, liberally allow reexamination of a jury's factual findings encourage appeals to be undertaken simply in the hope that another "fact

finder" might see things differently. This contributes not only to crowded dockets in the courts of appeals - and ultimately this Court - but, to the extent such standards permit properly instructed jury verdicts to be overturned, the efficient use of scarce judicial resources is frustrated. In the instant case, for example, eight weeks of trial for the litigants, the court, and the jury were rendered superfluous by an appellate court which decided to engage in its own independent fact finding, and yet another extensive trial will follow the remand. Such results cannot but adversely affect the perceptions of litigants and the public at large of the fairness and effectiveness of the administration of justice.

Thus, for both constitutional and juridical reasons, where there is disagreement over the proper standard of review, or where an improper one has been applied, this Court should exercise its jurisdiction to articulate the appropriate standard for appellate courts to follow.

B. There Is Disagreement in the Circuits Over the Standard of Review of Jury Findings on the Issue of Obviousness.

In *Graham v. John Deere Co.*, 383 U.S. 1 (1966), this Court explained the nature of the determination of nonobviousness required under § 103:

> While the ultimate question of patent validity is one of law. . . . the § 103 condition, . . . lends itself to several basic factual inquiries. Under § 103, the scope and content of the prior art are to be determined; differences between the prior art and the claims at issue are to be ascertained; and the level of ordinary skill in the pertinent art resolved. Against this

> background, the obviousness or nonobviousness of the subject matter is determined.

Id. at 17.

The determination of nonobviousness thus involves both questions of fact and questions of law, and the answers to the fact questions become the predicates upon which the legal answers must be based. When fact questions are submitted to and answered by a properly instructed jury, the Seventh Amendment requires that the answers given not be reexamined, except in accordance wth the principles of the common law. The proper standard for appellate review of jury-determined facts is the "substantial evidence" test: If the reviewing court finds substantial evidence supporting the jury's determination, it must be accepted and not otherwise questioned or "reexamined." *See Atlantic & Gulf Stevedores, Inc. v. Ellerman Lines, Ltd., supra,* 369 U.S. at 364; *International Terminal Operating Co., Inc. v. N. V. Nederl. Amerik Stoomv. Maats.,* 393 U.S. 74, 75 (1968) (per curiam).

In the context of patent law, and with particular regard to the question of nonobviousness, several circuits have recognized that jury-determined facts must be upheld on appellate review if supported by substantial evidence. *See, e.g., Velo-Bind, Inc. v. Minn. Mining & Mfg. Co.,* 647 F.2d 965, 971 (9th Cir.), *cert. denied,* —— U.S. ——, 102 S.Ct. 658 (1981) ("Although the conclusion of validity is ultimately one of law, the jury's findings of fact, which underlie this legal conclusion may not be overturned on appeal if supported by substantial evidence."); *Norfin, Inc. v. International Business Mach. Corp.,* 625

F.2d 357 (10th Cir. 1980); *Control Components, Inc. v. Valtek, Inc.*, 609 F.2d 763 (5th Cir.), *cert. denied*, 449 U.S. 1022 (1980); *Tights, Inc. v. Acme-McCrary Corp.*, 541 F.2d 1047 (4th Cir.), *cert. denied*, 429 U.S. 980 (1976).* Other circuits, however, appear to have ignored the strictures of the Seventh Amendment; they hold that the reviewing court may make its own independent analysis of the underlying facts and thus reexamine the jury's determinations unrestricted by the substantiality of the evidence supporting them. *See, e.g., Dual Manufacturing & Engineering, Inc. v. Burris Industries, Inc.*, 619 F.2d 660 (7th Cir.) (en banc), *cert. denied*, 449 U.S. 870 (1980); *Layne-New York Co. v. Allied Asphalt Co.*, 501 F.2d 405 (3rd Cir. 1974), *cert denied*, 421 U.S. 914 (1975).

Involving as it does both a critical part of the statutory test of patent validity and the precepts of the Seventh Amendment, this disagreement in the circuit courts of appeals over the proper standard of review for jury-de-

*The explication by the Fourth Circuit in *Tights, Inc. v. Acme-McCrary Corp., supra*, 541 F.2d at 1055-6 (citations omitted) was not followed by the Eighth Circuit in the instant case. It bears repeating here:

> We begin with the observation that the rules governing appellate review of patent cases are no different than in other types of civil litigation. . . . Thus, in determining whether the verdict in this case should have been directed, we must apply the same standard employed by the district court in passing on the original motion. . . . As such the question becomes whether there was sufficient evidence to support a verdict for the party opposing the motion. . . . In assessing the sufficiency of the evidence, however, our power of review continues to be limited by the Seventh Amendment, which provides that "no fact tried by a jury shall be otherwise reexamined in any Court of the United States, than according to the rules of the common law." . . . We may not, therefore, weigh the evidence, pass on the credibility of witnesses, or substitute our judgment of the facts for that of the jury. . . . Instead, we must view the evidence in light most favorable to the party against whom the motion is made, giving him the benefit of all reasonable inferences from the evidence.

termined facts in patent cases requires resolution by this Court. As is evidenced by the citations above, the conflicting decisions are of recent vintage and are spread throughout the circuits.

This case squarely presents the Court with an opportunity to resolve that disagreement by articulating the proper standard of review. The majority in the court below, recognizing the conflict of standards, (App. A, p. A-8), paid lip service to the substantial evidence test but proceeded to apply its own independent analysis to the evidence to arrive at factual determinations supportive of its erroneous conclusion that the Mitchell patent was invalid for obviousness. For example, although the jury had specifically determined in a special verdict that the inventions claimed in the Mitchell patent were not described in any of the documents encompassing the relevant prior art, (App. C, p. A-62, Special Verdict No. 16), the court of appeals, without reviewing the substantiality of the evidence supporting this jury determination, independently made the factual determination that "some sort" of a description of a particular claim was "inherent" in some prior art.* The court elsewhere independently concluded, again opposite to the findings of the jury, that the collinear configuration was "only logical" from the prior art. (App. A, p. A-14). Similarly, against the jury's findings, the court independently decided that the Mitchell patent teachings regarding a specific means for ac-

*"The Mitchell system claims a curing area and an unloading-overrun area on opposite sides of the manufacturing area in a collinear relationship. The Mortimer patent specification discusses a curing area or part of the plant where the slabs may set adjacent to a manufacturing area, and some sort of unloading area is inherent in any product manufacturing process based on an assembly-line format such as that disclosed in the Mortimer patent." (App. A, p. A-10).

curately moving and controlling the casting bed along the track were sufficiently described by prior art so that a person skilled in the art could practice the Mitchell invention."[10] (App. A, pp. A-12-A-13. *Compare* App. C, p. A-62, Special Verdict Nos. 16, 18).

Nowhere in its analysis of the factual issues on which its conclusion of invalidity is based does the court of appeals delineate the evidence supportive of the jury's special verdict findings and evaluate its substantiality. Rather, the court comments on the evidence it finds supportive of its own conclusion and presents that as independently derived facts.

Thus, as Judge Woods observed in dissent, the court in fact utilized an independent analysis approach, even while pretending to apply the substantial evidence test as well. (App. A, pp. A-29-A-30).[11]

Inasmuch as the reexamination of jury-determined facts is involved, which standard of review is applied is of serious moment. What the Eighth Circuit itself has recog-

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[10]In doing so, the court below also stepped outside of the record. It relied on U.S. Patent No. 3,354,786, (*see* App. A, p. A-13), which was not in evidence and was never designated part of the prior art by defendants under the statutory requirement of 35 U.S.C. § 282. In addition, the court below ignored the requirement of 35 U.S.C. § 112, which provides that a "means plus function" element in a patent claim shall be construed to cover the corresponding structure or acts described in the specification and equivalents thereof. Pursuant to this rule, the court below should have considered whether the *particular structure* of the means for moving the casting bed as described in the Mitchell patent appeared in the prior art, but it wholly failed to do so.

[11]Nor does the concurring opinion of Judge Arnold rehabilitate the court's analytical standard. Although he states that he does not read the court's opinion as giving no weight to the jury verdict, (App. A, p. —), he does not volunteer how or where the evidence is lacking in substantiality, nor can he change the independent evaluation which in fact took place as revealed by the opinion which he joined. If the concurrence means to offer the court's analysis as in fact constituting a substantial evidence review, then it is plain that the majority has misapprehended the nature of the test in a serious way.

nized with regard to the standard to be applied to factual determinations made by a *trial court* is, if anything, more true in the instant context of a *jury verdict:*

> "The entire responsibility for deciding doubtful fact questions in a nonjury case should be, and we think it is, that of the district court. The existence of any doubt as to whether the trial court or this Court is the ultimate trier of fact issues in nonjury cases is, we think, detrimental to the orderly administration of justice, impairs the confidence of litigants and the public in the decisions of the district courts, and multiplies the number of appeals in such cases."

Pendergrass v. New York Life Ins. Co., 181 F.2d 136, 138 (8th Cir. 1950) (Sanborn, J.)." As Judge Woods observed below in dissent, "once a proper demand for jury trial has been made and a jury trial is conducted, the appellate standards of review of a jury verdict should not be compromised because of the complexity of the issues presented." (App. A, p. A-30).

"Ironically, the Eighth Circuit has recently recognized, as both Judges Arnold and Woods acknowledge, that the proper standard for reviewing a *trial judge's* findings in a patent case is *not* independent analysis but the "clearly erroneous" standard. *See Contico Intern. v. Rubbermaid Commercial Prod.*, 665 F.2d 820 (8th Cir. 1981). Cf. App. A at pp. A-28, A-29. If Federal Rule of Civil Procedure 52(a) requires the clearly erroneous standard for trial court-determined facts, surely the Seventh Amendment is entitled to at least as much deference.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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